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Supreme Court of the United States

OCTOBER TERM, 1961

No. [redacted]

HARRY B. SMITH and MARY L. SMITH,

Petitioners,

vs.

UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI TO REVIEW THE JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

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UNITED STATES OF AMERICA.

PETITION FOR WRIT OF CERTIORARI TO REVIEW THE JUDGMENT OF THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT.

Petitioners, Harry B. Smith and Mary L. Smith, pray that a Writ of Certiorari issue to review the Judgment of the United States Court of Appeals for the Third Circuit entered in the above-entitled case on June 13, 1962.

Opinions Below.

The Opinion of the United States District Court for the District of New Jersey (R. 13a-18a)[1] is officially reported at 199 F. Supp. 208. The Opinion of the United States Court of Appeals for the Third Circuit is officially reported at 304 F. 2d 267 (pp. 26-30, *infra*).

Jurisdiction.

This case involves a suit for refund of income taxes for the years 1951 and 1952 (R. 5a-13a). The Judgment of the Court of Appeals was entered on June 13, 1962. Jurisdiction is conferred on this Court by 28 U. S. C., Section 1254(1).

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[1] References to the Record are to the page numbers of the Government's Appendix filed below. This Appendix constitutes the certified record, along with the Court of Appeals opinion and judgment.

Questions Presented.

1. Whether the date of passage of a retroactive amendment to the Internal Revenue Code can be permissibly construed as the date on which a tax was "paid", so as to deprive the intended beneficiaries of the amendment of relief by virtue of the statutory limitations on claims for refund?

2. Does not a retroactive amendment of the Internal Revenue Code impliedly repeal the statutory limitation on claims for refund where the amendment is rendered partially ineffective, at the date of its enactment, by virtue of a literal reading of these limitation provisions?

3. Is a tax correctly determined and paid, but subsequently decreed as overpaid by virtue of a statutory amendment, "erroneously or illegally assessed or collected", requiring compliance with the claim for refund provisions of the United States Code dealing with refunds of income taxes?

Statutes Involved.

Internal Revenue Code of 1939:

SEC. 117. CAPITAL GAINS AND LOSSES.

* * * * * * *

(q) [as added by Sec. 1 of the Act of June 29, 1956, c. 464, 70 Stat. 404] *Transfer of Patent Rights.*—

(1) *General Rule.*—A transfer (other than by gift, inheritance, or devise) of property consisting of all substantial rights to a patent, or an undivided interest therein which includes a part of all such rights, by any holder shall be considered the sale or exchange of a capital asset held for more than 6 months, regardless

of whether or not payments in consideration of such transfer are—

(A) payable periodically over a period generally coterminous with the transferee's use of the patent, or

(B) contingent on the productivity, use, or disposition of the property transferred.

* * * * * * *

(4) *Applicability.*—This subsection shall apply with respect to any amount received or payment made pursuant to a transfer described in paragraph (1) in any taxable year beginning after May 31, 1950, regardless of the taxable year in which such transfer occurred.

(26 U. S. C. 1952 ed., Sec. 117.)

SEC. 322. REFUNDS AND CREDITS.

[as amended by Sec. 172(e), Revenue Act of 1942, c. 619, 36 Stat. 798.]

(a) *Authorization.*—

(1) *Overpayment.*—Where there has been an overpayment of any tax imposed by this chapter, the amount of such overpayment shall be credited against any income, war-profits, or excess-profits tax or installment thereof then due from the taxpayer, and any balance shall be refunded immediately to the taxpayer.

* * * * * * *

(b) *Limitation on Allowance.*—

(1) *Period of limitation.*—Unless a claim for credit or refund is filed by the taxpayer within three years from the time the return was filed by the taxpayer or within two years from the time the tax was paid, no credit or refund shall be allowed or made after the expiration of whichever of such periods expires the later. If no return is filed by

the taxpayer; then no credit or refund shall be allowed or made after two years from the time the tax was paid, unless before the expiration of such period a claim therefor is filed by the taxpayer.

(26 U. S. C. 1952 ed., Sec. 322.)

Internal Revenue Code of 1954:

SEC. 6532. PERIODS OF LIMITATIONS ON SUITS.

(a) Suits by taxpayers for refund.—

(1) *General Rule.*—No suit or proceeding under section 7422(a) for the recovery of any internal revenue tax, penalty, or other sum, shall be begun before the expiration of 6 months from the date of filing the claim required under such section unless the Secretary or his delegate renders a decision thereon within that time, nor after the expiration of 2 years from the date of mailing by certified mail or registered mail by the Secretary or his delegate to the taxpayer of a notice of the disallowance of the part of the claim to which the suit or proceeding relates.

(26 U. S. C. 1958 ed., Sec. 6532 as amended by Pub. L. 85-866.)

SEC. 7422. CIVIL ACTIONS FOR REFUND.

(a) No Suit Prior to Filing Claim for Refund.—No suit or proceeding shall be maintained in any court for the recovery of any internal revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund or credit has been fully filed with the Secretary or his delegate, according to the provisions of law in that regard, and the regulations of the Secretary or his delegate established in pursuance thereof.

(26 U. S. C. 1958 ed., Sec. 7422.)

28 U. S. C.:

SEC. 1346 [As amended by Sec. 1, Act of July 30, 1954, 68 Stat. 589]. *United States as defendant.*

(a) The district courts shall have original jurisdiction, concurrent with the Court of Claims, of:

(1) Any civil action against the United States for the recovery of any internal-revenue tax alleged to have been erroneously or illegally assessed or collected, or any penalty claimed to have been collected without authority or any sum alleged to have been excessive or in any manner wrongfully collected under the internal revenue laws;

* * * * *

SEC. 2401. *Time for Commencing Action Against United States.*

(a) Every civil action commenced against the United States shall be barred unless the complaint is filed within six years after the right of action first accrues. The action of any person under legal disability or beyond the seas at the time the claim accrues may be commenced within three years after the disability ceases.

* * * * *

Statement.

The facts in this case are fully stipulated (R. 9a-13a).

The taxpayer prevailed in the District Court. The Government prevailed in the Court of Appeals.

Taxpayer, Harry B. Smith (hereafter referred to as the Petitioner)[2] and George A. Dolan were co-inventors and co-owners of two devices, described respectively as "Pipe Welding & Heat Treating Process", and "means

[2] Mary L. Smith is a co-petitioner, but solely because she filed a joint return with her husband for 1951 and 1952.

for Heat Treating and Welding Metal Parts". The former device was covered by United States Patent No. 2,184,534, issued to the inventors on December 26, 1939. An application for letters patent on the latter invention was executed by Petitioner and Dolan on December 18, 1946 (R. 19a).

Pursuant to an agreement executed on January 20, 1947 (hereinafter referred to as the 1947 agreement), Petitioner and Dolan, as licensors, granted an exclusive license to the aforementioned devices to Electric Arc, Inc., a New Jersey corporation, as licensee. In consideration, Smith and Dolan were to receive certain royalties based upon a percentage of the net sales price received for any electric heating apparatus or appliance manufactured, sold, or rented by the licensee. Neither Petitioner nor Dolan were ever employed by or owned stock in Electric Arc, Inc. (R. 10a-11a, 12a).

During 1951 and 1952, Petitioner received royalties under the 1947 agreement in the respective amounts of $49,784.12 and $37,975.43. On timely filed joint income tax returns for those years, Petitioner reported the amounts received as ordinary income (R. 11a-13a).

Section 117(q) was added to the Internal Revenue Code of 1939 by Section 1 of the Act of June 29, 1950, c. 464, 70 Stat. 404. The transfer of patent rights effected by the 1947 agreement fell within the class of transfers described in Section 117(q) (R. 11a, 13a-14a). This stipulated point eliminated all factual disputes in the case.

On July 15, 1958, Petitioner filed claims for refund of income taxes paid for 1951 and 1952. The basis of these claims was that the proceeds received under the 1947 agreement were properly reportable as long-term capital gains, and not as ordinary income. No administrative action was taken with respect to these claims within six months after they were filed, and, on February 20, 1959, Petitioner

instituted suit for recovery of the taxes in question (R. 11a, 13a). Jurisdiction was conferred upon the District Court by 28 U. S. C., Section 1346(a)(1).

In defense, the United States contended that inasmuch as Petitioner had failed to file refund claims within the time prescribed by the limitations provisions set forth in Section 322(b) (1) of the 1939 Code, the District Court, by virtue of Section 7422(a) of the 1954 Code, was without jurisdiction to hear the matter (R. 12a, 14a). The District Court rejected this contention and entered judgment for the Petitioner, holding that Section 117(q) had impliedly repealed the existing statutory bar. Alternatively, the District Court held that Section 117(q) created a new cause of action in favor of the Petitioner, and, therefore, that the period prescribed in Section 322(b) (1) did not begin to run until June 29, 1956, when Section 117(q) was enacted (R. 13a-19a).

The United States appealed the judgment of the District Court to the United States Court of Appeals for the Third Circuit. For this appeal, jurisdiction was conferred upon the Court of Appeals by 28 U. S. C., Section 1291.

The Court of Appeals reversed the judgment of the District Court and had the cause remanded with directions to proceed in accordance with its opinion.

The opinion of the Court of Appeals made two determinations:

(1) The Act of June 29, 1956 (Section 117(q)) created a constructive payment of tax as of the date the Act was approved; and, consequently, the limitation of Section 322(b)(1) of the 1939 Internal Revenue Code for filing claims for refund "within two years from the time the tax was paid" began to run June 29, 1956 and expired on June 28, 1958—prior to petitioner's filing of his claims for refund on July 15, 1958; and

(2) The Act of June 29, 1956 did not repeal Section 322(b)(1) to the extent of any alleged repugnancy between the two statutes.

Other questions raised by both parties were not decided as these two determinations were conceived to be dispositive.

Summary of Argument.

The Petitioner contends that a claim for refund of income taxes filed within 3 years from the creation of the right (the enactment of Section 117(q)) is a claim filed "according to the provisions of law." The Third Circuit found (implausibly, it would seem) that the enactment of Section 117(q) was a "constructive payment". And because it was a "payment" the shorter 2 year statute applied. Such reasoning denied the timeliness of the refund by 18 days. This interpretation of legislative intent is contrary to the accepted liberal standard which has been applied to taxing statutes, *including the limitations periods embodied therein*, by the Supreme Court, the Second Circuit, the Tenth Circuit, and the Court of Claims. It is consistent, however, with opinions of the Fifth and Sixth Circuits, as well as other non-reconciled decisions of the Court of Claims. The Petitioner seeks the logical and required liberal construction of "the provisions of law". He also urges the importance of achieving judicial uniformity in such a basic area.

However, even if the "constructive payment" theory of the Third Circuit were to be hypothetically accepted, the limitation period on claims for refund (Section 322(b)(1)) should be construed as impliedly repealed by Section 117(q) to the extent of any repugnancy. Section 117(q)(4) expressly applies to 1951 and 1952; yet it was

enacted in 1956. It is clear that no ordinary limitation period for refunds was intended to apply for these years. There is a repugnancy existing here which requires the application of this doctrine of implied repeal.

Yet the Third Circuit has somehow found authority to figuratively re-enact Section 322(b)(1); but this time as a limiting factor running not from a filed tax return or actual payment, but from the date of the passage of Section 117(q). This treatment is unsupported by valid precedent.

Finally, assuming the "constructive payment" and discounting the implied repeal, again for presentation purposes only, the type of refund involved here does not involve an "illegal" or "erroneous" assessment or payment. The tax paid, at the time of payment, and until the enactment of Section 117(q), was quite correct and legal. Without illegality, error, or overpayment, there can be no literal compliance with Section 7422(a), which requires a claim for refund as a precondition to suit only when "erroneous" or "illegal" assessments are involved. The basis of the Government's case is essentially Petitioner's non-compliance with Section 7422(a). This basis becomes diluted when analyzed in this context.

All three areas are recurring and important. They deal with the administration of the Internal Revenue laws in general, and the troublesome effect of a retroactive amendment in particular. There is hardly a uniform view from the various courts of appeal or from the trial courts. It is urged that the granting of a Writ of Certiorari is warranted.

ARGUMENT.

POINT 1.

The Court of Appeals ruled erroneously when it construed the enactment of a statute to be a payment.

The statute in question[3] was enacted to equalize the treatment to inventors under the 1954 and 1939 Internal Revenue Codes. The 1954 Code provision[4] had greatly altered previous regulatory, decisional, and statutory law surrounding patent licensing. Section 117(q), enacted on June 29, 1956, accomplished the same result retroactively for the 1939 Code.

Previous to this legislation, patent royalties based on a percentage of sales payable over the life of the patent, had been taxable as ordinary income.[5] Also sums received by a professional inventor for the sale of his patent had been considered ordinary income.[6] Similarly, the holding period required for *long*-term capital gain treatment on the sale of patents by an amateur inventor had previously been a minimum of six months.[7]

All of these situations have been changed. By its terms, Section 117(q) has removed the "periodic payment" taint, abolished the requirement for amateurism[8], and has fixed

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[3] Act of June 29, 1956, c. 463, 70 Stat. 404. See 1; 26 U. S. C. Sec. 117 (q) Int. Code of 1939.

[4] 26 U. S. C. Sec. 1235, Int. Rev. Code of 1954

[5] Mim. 6490, 1950-1 Cum. Bull. 9

[6] 26 U. S. C. Sec. 61 (a) (3) and (6), Int. Rev. Code of 1954

[7] 26 U. S. C. Sec. 1222 (3), Int. Rev. Code of 1954

[8] 26 U. S. C. Sec. 117 (q) (1) (A) and (B); S. Rep. No. 1622, 83rd Cong. 2d Sess., 3 U. S. C. Cong. and Adm. News 1954, 4621, 5081-5084

[9] *Ibid.*

no holding period at all for long-term capital gain treatment.[10]

This was clearly a tax-relief statute intended to grant retroactive benefits. It had been enacted two years after the last effective date of the 1939 Code. It had been actually conceived of as more than tax relief. It had also tried to encourage activities of inventors by giving them a favored treatment prospectively, which hardly seems a revenue function. A landowner in the business of selling land realizes ordinary income upon the profitable sale of this land. The same with a car-owner or a junk-dealer or any class of taxpayers engaged in their trade or business. Not so with inventors.

A reading of the various reports on Section 1235 of the 1954 Code confirms this. The House Report is significant even though the bill emanating from the House was changed by the Senate. The House report states:

> "Under existing law, only amateur as distinguished from professional inventors can obtain capital gain treatment; and, to make this distinction it has become necessary to determine whether sufficient prior inventions exist to warrant placing the taxpayer in the business of selling inventions to customers, a requirement that in many instances caused confusion and litigation. To obviate this difficulty in the case of gain, and to provide a larger incentive to all inventors to contribute to the welfare of the nation, this section is applicable to all inventors, whether amateur or professional, regardless of how often they sell their patents." H. Rep. No. 1337, 83rd Cong. 2nd Sess.; 3 U. S. C. Cong. and Adm. News (1954) 4017, 4421 to 4424 at p. 4422.

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[10] The provisions of Section 117 (q) 1 state that the "gain, if" of such "property" "shall be *considered* the sale . . . of a capital asset held for more than 6 months . . ." without apparent requirement of proof of holding period.

The Senate report, which had fashioned the final statute, is just as revealing:

> "This section is an extensive revision of Section 1235 of the House Bill. It has no counterpart under existing law . . . .
>
> "Under present law . . . an exclusive license of the right to manufacture, use, and sell, the invention . . . can qualify as a 'sale or exchange' for tax purposes; thus, the holder can obtain capital-gains treatment on such a transfer if he falls within the 'amateur' category. Many court decisions have arrived at this result. . . . Edward C. Myers, 6 T. C. 258 (1946). Non Acq. 1950-1 Cum. Bull. 9. . . . To obviate the uncertainty caused by this . . . [non-acquiescence of Myers] and to provide an incentive to inventors to contribute to the welfare of the Nation, your committee intends, in subsection (a) to give statutory assurance to certain patent holders that the sale of a patent . . . shall not be deemed not to constitute a 'sale or exchange' for tax purposes solely on account of the mode of payment . . . .
>
> "[T]he section does apply to all qualifying individuals, whether amateur or professional, regardless of how often they have sold their patents." S. Rep. No. 1622, 83rd Cong. 2d Sess.; 3 U. S. C. Cong. and Adm. News (1954) 4621, 5081-5084.

The standard to be applied in interpreting such tax statutes is a liberal one. Section 117(q) should not be an exception. Such statutes "should be construed in favor of those intended to be benefited." *Hollander v. United States*, 248 F. 2d 247, 251 (2 Cir. 1957).

> "In case of doubt, they are to be construed most strongly against the government, and in favor of the citizen." *Gould v. Gould*, 245 U. S. 151, 153 (1917).

This theory has been frequently cited. In *United States v. Updike*, 281 U. S. 489 (1929), the Court held for the taxpayer by broadly and liberally interpreting a clause which had required governmental action to be prompt or face the alternative of being unable to collect the tax. In describing its finding which restricted the Government, the Court stated:

> "[W]e think this is a fair interpretation of the clause, and the one which must be accepted, especially in view of the rule which requires taxing acts, *including provisions of limitation embodied therein*, to be construed liberally in favor of the taxpayer. *Bowers v. New York & A. Lighterage Co.* 273 U. S. 346, 349, 71 L. Ed. 676, 678, 47 Sup. Ct. Rep. 389." *Id.* 281 U. S. at 496 (emphasis supplied)

The Tenth Circuit has followed identical reasoning. *Commissioner v. Wilson* 60 F. 2d 501 (10 Cir. 1932).

As an illustration of the specific application of this rule, the Revenue Act of 1921[11] had granted estate tax relief to property previously taxed within five years. It had provided for a deduction of said prior tax "in the case of estates of all decedents who have died since September 8, 1916." In a suit relying on this Act, the Court of Claims would not fault a claim for refund filed 12 years after the payment of the tax, and 11 years after the enactment of this relief provision. It permitted the claim as a valid basis for the suit. *Siegel v. United States*, 18 F. Supp. 771 (Ct. Cl. 1937); *cf. Detroit Trust Co. v. United States* 18 F. Supp. 776 (Ct. Cl. 1937). The then equivalent of Section 322(b)(4) was completely disregarded:

> "It is clear from these sections that Congress intended that all estates which had paid a tax by reason of the inclusion in the net estate of property

[11] Sections 403 (b) (2) and (3) of the Revenue Act of 1921.

> which had been previously taxed within five years should be entitled to have the benefit of this deduction, the tax redetermined and the excess tax refunded *without regard to the limitation of* time within which the Commissioner of Internal Revenue could make a refund without a claim, or the *time within which claims for refund could be filed* under §3228, Revised Statutes (26 U. S. C. A. §1433) [similar to Section 322(b)(1) of the 1939 Internal Revenue Code]. The Commissioner has correctly so held in Article 99 of Regulations 70." 18 F. Supp. at 773. (emphasis supplied)

Interpretively, the Court of Claims is precisely in conflict with the Third Circuit; and the Second and Tenth Circuits are, at the very least, conceptually opposed to the Third Circuit. The Supreme Court also has had an evidently different approach to the enforcement of such statutes.

To be sure, the Third Circuit does not stand alone in this construction favoring the Government. The Fifth Circuit, *Tobin* v. *United States* 264 F. 2d 845 (1959), and the Sixth Circuit, *United States* v. *Dempster* 265 F. 2d 666 (1959), *cert. den.* 361 U. S. 819, reached similar results. Indeed, the Court of Claims, without attempting to reconcile the earlier *Siegel* and *Detroit Trust Co.* cases, apparently adopted this "constructive payment" theory as a limiting factor in *Lorenz* v. *United States* 296 F. 2d 746 (1961), and probably does the same in the otherwise favorable opinion on the identical statute in *Zacks* v. *United States*, 280 F. 2d 829 (1960)[12]; see also *Eastman Kodak Co.* v. *United States* 292 F. 2d 901 (Ct. Cl. 1961).

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[12] The Zacks case does mention approvingly that *suit* was instituted within 2 years from the enactment of Section 117(q) (280 F. 2d at 830); however, suit can permissibly be instituted any number of years after a claim for refund is filed if the Government fails to disallow the claim (26 U. S. C. Sec. 6532(a)).

The holding of the Third Circuit, as well as the other aligning decisions, overrode this basic presumption applied to all tax measures, not to mention statutes giving non-tax relief. The Third Circuit has applied the legislation in a negative manner to an area afforded positive relief.

Specifically, the finding that the enactment of a statute is a "constructive payment" is an unwarranted straining of Congressional intent. The Petitioner had made no payments, constructively or otherwise, on June 29, 1956. Nothing in the legislative history indicates Congress had intended this to be the case. The Petitioner had made his payments when he filed his returns on March 15, 1952 and March 15, 1953. His right to the refund arose on June 29, 1956.[13] To foreshorten the period within which he was obliged to proceed on this right by reading this unnatural construction into the statute has done a serious disservice to legislative purpose.

Section 322(b)(1) requires that a claim for refund be filed within three years from the date the return is due or two years from the date of payment "whichever of such periods expires the later." The finding of a "constructive payment" by the dialectics adopted in the opinion below was an artificial, non-purposeful judicial fiat. The intent of Congress had been manifestly to lessen the tax burden on inventors. How much more logical then would have been the acceptance of the period which "expires the later" (or 3 years) rather than defeating legislative purpose and decisional principle by applying the shorter period, especially when it has been based on such attenuated reasoning.

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[13] The Third Circuit accepted this premise, *arguendo*, p. 29 *infra*.

If the situation were clearly within the two-year "payment" period, this presumption or rule of construction would admittedly serve no purpose. But here the Third Circuit has formulated this dubious unclear conclusion, and deprived the Petitioner by 18 days of his unquestioned right.[14] The District Court seemed more cognizant of the unreality of such reasoning.[15] The District Court's holding was correct. The *Siegel* and *Detroit Trust Co.* cases are correct, as is the reasoning of *Gould, Updike, Hollander,* and *Wilson.*

This basic problem in the construction of the Revenue Laws should be finally resolved so as to avoid the disparate holdings that can and have resulted in the various circuits (in particular, the Second, Third, Fifth, Sixth and Tenth), and in the oft-cited and respected Court of Claims.

POINT 2.

A subsequently enacted statute repeals by implication an existent statute to the extent that the subsequent one is clearly repugnant to the existent one, and the Court of Appeals erred in failing to apply this principle.

Section 117(q)(4) states that the beneficial provisions of Section 117(q)(1) "shall apply . . . in any taxable year beginning after May 31, 1950. . . ."

Section 322(b)(1) states that "unless a claim for . . . refund is filed . . . within three years from the time the return was filed or within two years from the time the tax was paid, no credit or refund shall be allowed or made. . . ."

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[14] If we accept the Third Circuit's reasoning, the right to file a valid claim for refund expired June 27, 1958. The claim was filed July 15, 1958.

[15] R. 13a-18a.

Section 117(q) was enacted on June 29, 1956. If we apply Section 322(b)(1) literally, no limitation period (3 or 2 years) could possibly cover a claim filed for 1951 or 1952 returns filed timely. Yet Section 117(q)(4) specifically applies to the years 1951 and 1952 (among others). This conflict appears irreconcilable.

The Government had earlier contended that Section 117(q) was enacted merely to clarify the rights of taxpayers then involved in the administrative or judicial process who had previously signed waivers of the statute of limitations, filed claims for refund, or instituted suits in the courts.[16] The Petitioner had contended that this was a seemingly illogical interpretation due to the fact that this would benefit only taxpayers who had seen fit to oppose the Commissioner's announced position.[17] The Petitioner also had pointed out that Section 117(q) did more than clarify pre-existing law; it greatly *changed* the law.[18]

In any event, the Third Circuit has avoided this issue by conceding the Petitioner's position, *arguendo*, and observing that even if this were so, the claims for refund were still not timely. It then went on to state:

> "We, of course, recognize that, inherent in our disposition is a holding that we do not agree with taxpayer's view that the Act of June 29, 1956 repealed Section 322(b)(1) to the extent that it obliterated any and all statutory limitations with respect to claims for tax refunds relating to patent royalties." (p. 30 *infra.*)

This quoted sentence generally states the Petitioner's position. However, the Third Circuit has painted the Petitioner's argument in broader strokes than were urged.

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[16] See the Government's brief below pp. 26-29.

[17] See n. 5, *supra.*

[18] See the Petitioner's brief below pp. 12-18.

The Petitioner had maintained, and does maintain, that the Act of June 29, 1956 repealed Section 322(b)(1) *to the narrow extent of any existent repugnancy.*[19] It has never been contended that "any and all statutory limitations" were thus "obliterated." This misconception of the Petitioner's position was itself unfortunate; and if the Court of Appeals derived support for its findings from such an over-generalized and ill-advised contention, an injustice was done the Petitioner.

In essence, the Petitioner's view has previously been stated by the Supreme Court:

> "Where there are two acts upon the same subject, effect should be given to both if possible. There are two well-settled categories of repeals by implication—(1) *where provisions in the two acts are in irreconcilable conflict, the latter act to the extent of the conflict constitutes an implied repeal of the earlier one;* and (2) if the latter act covers the whole subject of the earlier one and is clearly intended as a substitute, it will operate similarly as a repeal of the earlier act." *Posadas* vs. *National City Bank* 296 U. S. 497, 503 (1936). (Emphasis supplied.)

An earlier case had stated that if two acts—

> "are repugnant in any of their provisions, *the latter act, without any repealing clause, operates to the extent of the repugnancy as a repeal of the first;* and even where two acts are not in express terms repugnant, yet if the latter act covers the whole subject of the first, and embraces new provisions, plainly showing that it was intended as a substitute for the first act, it will operate as a repeal of that act." *United States* vs. *Tynen*, 78 U. S. (11 Wall.) 88, 92 (1870). (Emphasis supplied.)

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[19] See the Petitioner's brief below pp. 4-12.

See also *Dariess* v. *Fairbairn*, 44 U. S. (3 How.) 636 (1845); *In re Henderson's Tobacco*, 78 U. S. (11 Wall.) 652 (1870); *United States* v. *Tingey*, 30 U. S. (5 Pet.) 115 (1831).

A district court has adopted this theory of *pro tanto* repeal of the very statute with which we are dealing. In *Field's Estate* v. *United States*, 131 F. Supp. 76 (S. D. N. Y. 1955), the court found that there was an implied repeal of the 1954 Code equivalent of Section 322(b) (1). Otherwise a certain section of the Revenue Act of 1951 would have afforded relief which was paradoxically unattainable as a result of this statutory strait jacket.

As applied to this case, the *pro tanto* repeal of Section 322(b) (1) would eliminate the need to file refund claims on or before 3 years *from the filing of the returns*. This has become, in some cases, an accepted interpretation: *Lorenz* v. *United States*, 296 F. 2d 746 (Ct. Cl. 1961); *Zacks* v. *United States*, 280 F. 2d 829 (Ct. Cl. 1960); *contra*, *Tobin* v. *United States*, 264 F. 2d 845 (5 Cir. 1959); *United States* v. *Dempster*, 265 F. 2d 666 (6 Cir. 1959), *cert. den.* 361 U. S. 819. See also *Vaughn* v. *United States*, 181 F. Supp. 386 (S. D. Cal. 1960). In any event the Third Circuit in this case has accepted this interpretation.

If such a repeal did take place, there is hardly justification for their reinstating the very section thus repealed as a delimiting statute for an event other than a filed return or a payment, *i.e.*, the enactment of a tax relief measure. If it is ineffective as a bar in reference to a filed return, how can it become revitalized as a limitation to an event never conceived of by Congress—the passage of Section 117(q)?

We are faced with the repugnancy of Section 117(q) and 322(b) (1). It falls squarely within the ambit of a statute being impliedly repealed to the extent of this repug-

nancy. If this is so, wherein has the Third Circuit acquired the legislative ability to re-enact Section 322(b) (1) as a bar to claims running from the enactment of a statute?

The short shrift made of implied repeal by the Court of Appeals has failed to recognize the significance of and precedent for this view. The District Court appreciated the linguistic impossibility of literally applying Section 322(b) (1) as to the years 1951 and 1952 when the implementation of Section 1170(q) (1) was being sought. The way out of this dilemma is reliance on this rule of statutory construction. The solution is logical and legally justified.

The Third, Fifth, and Sixth Circuits (*i.e., Smith, Tobin,* and *Deutpster* respectively) have either directly or impliedly rejected the validity of this principle.

This Court should now articulate the soundness and present applicability of the doctrine of repeal by implication. Apparently previous pronouncements by this Court have not been consistently respected.

POINT 3.

The claim for refund provisions do not apply to taxes which were not "erroneously or illegally assessed or collected."

The real basis of the Government's case has been the alleged failure of the Petitioner to comply with Section 7422(a) of the 1954 Internal Revenue Code. Let us assume, *arguendo*, that there was no compliance. This section states that:

> "No suit . . . shall be maintained in any court for the recovery of any internal revenue tax *alleged to have been erroneously or illegally assessed or collected* . . . until a claim for refund . . . has been

fully filed with the Secretary or his delegate, according to the provisions of law in that regard, and the regulations of the Secretary or his delegate, established in pursuance thereof." (Emphasis supplied)

The Government has argued that because the claim for refund was not filed "according to the provisions of law [Section 322(b)(1)]", Section 7422(a) was not complied with.

Taken literally, and there is no reason to suppose Congress intended otherwise,[20] the cited Section has really no application here.

The tax paid by the Petitioner in 1951 and 1952 had been commendably correct and legal. Section 117(q) finally gave Petitioner the right to claim an overassessment, but this accrued in 1956. Can we ever say that this was an "erroneous" or an "illegal" assessment or collection?[21]

The Supreme Court has passed on a similar, but distinguishable, issue. In *Jones v. Liberty Glass Company*, 332 U. S. 524 (1947), the taxpayer had argued the applicability of a 4-year statute instead of the present 2 years of Section 322(b)(1) as applied to payments. The taxpayer claimed that it was the error of the revenue agent on an examination that resulted in the overpayment and not the error of the taxpayer. Through somewhat involved reasoning, the taxpayer contended that the revenue agent's errors were not the "erroneous or illegal assessments" embraced by Section 322(b)(1); and, therefore, that section was not applicable. The Court disagreed. It proceeded to define "overpayment" as covered by Section 322(b)(1):

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[20] See, *e.g.* The Hanover Bank v. Commissioner, 369 U. S. 672 (1962); Crane v. Commissioner, 331 U. S. 1, 6, 14[6].

[21] It must be remembered that the Third Circuit accepted, *arguendo*, the premise that Section 117(q) created a new right (p. 29 *infra*).

"Hence we use the word 'overpayment' in its usual sense, as meaning any payment in excess of that which is properly due. Such an excess payment may be traced to an error in mathematics or in judgment or in interpretation of facts or law. And the error may be committed by the taxpayer or by the revenue agent. *Whatever the reason, the payment of more than is rightfully due is what characterizes an overpayment.*" 332 U. S. at 531 (emphasis supplied)

It is with this reasoning in mind that the judgment of the Court,[22] confining all income tax refunds to Section 322(b)(1), should be analyzed. This is especially true when it is noted that the taxpayer in *Jones* v. *Liberty Glass Company* had been specifically relying on the fact that the income tax he had paid was "erroneously or illegally assessed or collected,"[23] (but not bound by Section 322 (b)(1)); whereas the herein Petitioner has steadfastly maintained his correctness *and* the Commissioner's correctness, until the passage of Section 117(q).

The thing that characterizes an "overpayment" is paying "more than is rightfully due". There has never been an overpayment in this case.

Where then does that leave the Petitioner? He still had attempted, where possible, to follow established procedures for obtaining an income tax refund.

He had filed a claim for refund (Form 843). He had waited 6 months before instituting suit (Section 6532(a) 1954 Internal Revenue Code). He had relied for jurisdiction upon the tax refund section (28 U. S. C., Section 1346(a)(1)).[24]

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[22] *Id.* 332 U. S. at 534-535.

[23] *Id.* 332 U. S. at 535.

[24] See Amended Complaint (R. 2a)

In regard to Section 1346(a)(1), it is not surprising to find language identical to Section 7422(a) of the 1954 Code. The former states.

> "The district courts shall have original jurisdiction . . . of . . . any civil action against the United States for the recovery of any internal-revenue tax alleged to have been erroneously or illegally assessed or collected. . . ."

There is no invalidating inconsistency in this. After all, what is involved is income tax; and the Petitioner is seeking a refund of it. There would have been no other way to bring his claim to court. It is not a suit on open account. The enactment of Section 1346(a) had not been intended as a right without a remedy.

What the Petitioner has done here is follow as closely as he can the traditional claim for refund procedures.

The Petitioner has invoked the District Court's jurisdiction on tax refund suits. Only a strict reading of Section 1346(a)(1) would deny him jurisdiction. His reliance on 28 U. S. C. Sec. 1346(a)(1) should be liberally construed. *cf. United States* v. *Shaw*, 309 U. S. 495 (1939).

In urging this point, the Petitioner is not unmindful of certain Court of Claims decisions which have dealt with this problem. *Eastman Kodak Co.* v. *United States*, 292 F. 2d 901 (1961), *overruling Westinghouse Electric Corp.* v. *United States*, 140 F. Supp. 565 (Ct. Cl. 1956). These cases had involved subsequent fact changes which entitled the taxpayers to refund.[*] No "error" or "illegality" had been even remotely involved. *Westinghouse* stated that because no erroneous or illegal overassessments ever took

[*] In *Westinghouse*, the taxpayer incurred long-term warranties which resulted in a reduction of sales, and thus a right to refund of excise taxes. In *Eastman Kodak*, the taxpayer reached the same result by making price adjustments on previous sales. . . .

Opinion of the Court of Appeals.

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 13,728

HARRY B. SMITH AND MARY L. SMITH

v.

UNITED STATES OF AMERICA,
Appellant

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEW JERSEY

Argued January 11, 1962

Before BIGGS, *Chief Judge* and KALODNER and GANEY, *Circuit Judges*

OPINION OF THE COURT

(Filed June 13, 1962)

KALODNER, *Circuit Judge*

This appeal by the United States presents the issue as to whether the District Court erred in rendering judgment for the taxpayer, Harry B. Smith,[1] in his suit for refund of income taxes paid for the years 1951 and 1952 on patent

[1] The opinion of the District Court is reported at 192 F. Supp. 9 (D. N. J. 1961).

royalties which were treated as ordinary income pursuant to then current rulings of the Commissioner of Internal Revenue.

Taxpayer's suit for refund was premised on the Act of June 29, 1956 (70 Stat. 404) which amended the Internal Revenue Code of 1939 by adding Section 117(q)* which provided that royalties of the type here involved were to be considered as capital gains, and made its provisions applicable to all royalty payments received after May 31, 1950.

In his suit for refund, filed February 20, 1959, taxpayer alleged that on July 15, 1958 he had filed his claims for refunds for overpayment of taxes for 1951 and 1952 and that the Commissioner of Internal Revenue had taken no action with respect thereto.

In defense, the United States contended that the District Court was without jurisdiction of the subject matter under Section 7422(a) of the Internal Revenue Code of 1954† because the claims for refund were not filed within

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* Section 117(q) reads in relevant part as follows:

"(q) Transfer of patent rights—

"(1) General rule.—A transfer (other than by gift, inheritance or devise) of property consisting of all substantial rights to a patent, or an undivided interest therein which includes a part of all such rights, by any holder shall be considered the sale or exchange of a capital asset held for more than 6 months, regardless of whether or not payments in consideration of such transfer are—

. . . . . .

"(4) Applicability.—This subsection shall apply with respect to any amount received or payment made pursuant to a transfer described in paragraph (1) in any taxable year beginning after May 31, 1950, regardless of the taxable year in which such transfer occurred."

three years from the time the returns were filed or within two years from the time the taxes were paid, as specified in Section 322(b)(1) of the Internal Revenue Code of 1939.[3]

The District Court, in rejecting the Government's contention and granting recovery to taxpayer, held that (1) the limitation provisions of Section 322(b)(1) of the 1939 Code and Section 7422(a) of the 1954 Code were impliedly repealed by the Act of June 29, 1956, and, (2) alternatively, the 1956 Act created a new cause of action for refund upon which the statute of limitations commenced to run anew.

On this appeal the United States urges that the District Court erred in the holdings stated, and, that even assuming that the 1956 Act created a new cause of action, taxpayer's suit is nevertheless barred by his failure to file refund claims within two years after June 29, 1956 as Sec-

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erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected, until a claim for refund or credit has been duly filed with the Secretary or his delegate, according to the provisions of law in that regard, and the regulations of the Secretary or his delegate established in pursuance thereof."

[3] Section 322(b)(1) of the Internal Revenue Code of 1939 provides:

"Unless a claim for credit or refund is filed by the taxpayer within three years from the time the return was filed by the taxpayer or within two years from the time the tax was paid, no credit or refund shall be allowed or made after the expiration of whichever of such periods expires the later. If no return is filed by the taxpayer, then no credit or refund shall be allowed or made after two years from the time the tax was paid, unless before the expiration of such period a claim therefor is filed by the taxpayer."

tions 322(b)(1) and 7422(a) would require. The claims for refund, as earlier noted, were filed July 15, 1958.

The sum of taxpayer's contention here is (1) the District Court did not err, (2) the procedural requirements of Sections 322(b)(1) of the 1939 Code and 7422(a) of the 1954 Code are not applicable since Section 117(q) is a "nontitle act" of Congress and not an integral part of the revenue system and accordingly claims created by it are controlled by the general six-year statute of limitations as to suits against the United States; and (3) if the limitation provisions of Section 322(b)(1) are applicable the period is three years and not two years, and since the claims for refund here were filed within three years they are not barred.

It would serve no useful purpose to explore the arguments made by the parties in support of, and contra to, the District Court's holding that Section 117(q) of the Act of June 29, 1956 created a new cause of action[1] inasmuch as we agree with the Government's contention that assuming it did so, taxpayer's claims for refund are barred because they were filed on July 15, 1958—more than two years after June 29, 1956.

The decisions which have held that the Act of June 29, 1956 created a new cause of action have subscribed to the theory that it also created a constructive payment of the tax as of the date the Act was approved. That being so, the limitation of Section 322(b)(1) for the filing of a refund claim "within two years from the time the tax was

[1] The Court of Claims holds to the view that Section 117(q) creates a new cause of action. Lucas v. United States, 296 F.2d 746 (1961); Zacks v. United States, 295 F.2d 829 (1961), while the United States Court of Appeals for the 9th Circuit in Tobin v. United States, 261 F.2d 815 (1959), and that of the 5th Circuit in United States v. Donahue, 285 F.2d 666 (1960), cert. den. 366 U. S. 919 subscribe to contrary view. See also Vaughn v. United States, 184 F. Supp. 386 (S. D. Cal. 1959).

paid" began to run on June 29, 1956 and expired on June 28, 1958—prior to taxpayer's filing of his refund claims on July 15, 1958.

We, of course, recognize that inherent in our disposition is a holding that we do not agree with taxpayer's view that the Act of June 29, 1956 repealed Section 322(b)(1) to the extent that it obliterated any and all statutory limitations with respect to claims for tax refunds relating to patent royalties.

We might add that we do not construe the District Court's opinion to express agreement with taxpayer's view on this score. If it did so we would be constrained to rule it to be in error.

For the reasons stated the judgment of the District Court in favor of taxpayer and against the United States will be reversed and the cause remanded with directions to proceed in accordance with this opinion.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit